Southwestern Vermont Medical Center
Operating Budget
Fiscal Year 2016

Southwestern Vermont Medical Center's (hereafter "SVMC" or "Medical Center") Operating Budget for Fiscal Year (hereafter "FY") 2016 has a planned operating gain of approximately $4.4 million or an operating margin of approximately 3.0%. The excess of revenues over expenses including non-operating activities is nearly $5.0 million.

Below is a high level summary:

	FY 2015 Projected	***FY 2015 Budget***	***FY 2016 Budget***
Net patient service revenues	$140,468,617	$139,041,542	$144,025,571
Other operating revenues	2,012,534	1,986,231	2,022,823
Total operating revenues	*142,481,151*	*141,027,773*	*146,048,394*
Operating expenses	*138,256,990*	*136,806,217*	*141,665,762*
Operating gain	***4,224,161***	***4,221,556***	***4,382,632***
Non-operating revenues-net	749,827	575,000	600,000
Excess revenues over expenses	***$4,973,998***	***$4,796,556***	***$4,982,632***

The FY 2016 budgeted operating revenues are $5,020,621 more than the FY 2015 budget. Net patient service revenues are $4,984,029 or 3.6% more than the FY 2015 budget.

Below are summary points of material interest included in the budget:

- The budget includes expanded primary care services in Pownal, Express Care on the Bennington campus, as well as the addition of an existing Family Medicine practice in Bennington. Enhancing services in Palliative Care, Allergy and Rheumatology practices and the addition of a new Neurology practice;

- Medicare Sole Community Hospital (hereafter "SCH") program has been budgeted for the full fiscal year and is an increase of $2.2 million over FY 2015 budgeted revenue;

- Inpatient and Same Day Surgery volumes are budgeted to decline. Outpatient and Physician Services continue to increase;

- Medicaid reimbursement rates will ***not*** be increased as instructed by the Green Mountain Care Board (hereafter "GMCB"), at this time;

- The effective charge / rate increase of 3.8% is being requested;

- Vermont Disproportionate Share Payments (hereafter "DSH") are budgeted at $1,856,351 or a decrease from FY 2015 amount by approximately $933,000;

- Included in the budget is an increase in Medicare reimbursement for FY 2016;

- Full Time Employee Equivalents (hereafter "FTE's") of 747.9 are 13.3 FTE's higher than FY 2015's budget;

- A 3% salary increase was included, effective May 2016;

- Included in the supply cost are budgeted to decrease by approximately $653,000 due to the continued qualifying for the federal "340b" drug discount program and a reduction in chargeable medical supply cost due to the reduction of orthopedic surgical volume as well as others;

- The FY 2016 Capital Budget is $17,160,000.

Below are explanations of the changes to the FY 2016 budget when compared to the FY 2015 budgeted amounts.

<u>Gross Patient Service Revenues</u>

Total gross charges in the FY 2016 budget are increasing by $6,553,568 or approximately 2.2%.

Effective rate increase of 3.8%	$11,138,107
Expanded, enhanced primary care services	2,285,264
Other medical practice changes	(4,193,902)
Subtotal	*9,229,469*
Volume and payer mix changes	(2,675,901)
Total change in gross patient service revenues	***$6,553,568***

The explanations to the changes in gross patient service revenues will be discussed in the net patient service revenues section.

Net Patient Service Revenues

The increase in FY 2016 net patient service revenues budget is $4,984,029 or an increase of 3.6% when compared to FY 2015's budget.

In the development of the FY 2016 the table below lists the significant items:

Charge/rate increase to be realized *(effective rate 3.8%)*	$3,088,136
Medicare rate increases	518,392
Medicare Sole Comm. Hospital -- SCH reimbursement	2,200,000
Decrease in Medicaid DSH payments	(932,945)
Decrease indigent care (bad debt and charity care)	1,010,000
Expanded access, enhanced services and new practice development	1,222,779
Subtotal	*7,106,362*
Other practice volume changes	(618,768)
Volume and payer mix changes	(1,503,565)
Total change in net patient service revenues	***$4,984,029***

The rate increase is budgeted at 3.8%

Realization of the charge increase of 3.8% is dependent on commercial insurance, Blue Cross and managed care volumes and the mix of services. Prior to the start of the budget process the Hospital reviewed its charge structure and determined that not all charge categories should be increased in the FY 2016 budget. It was determined that physician professional services, drugs sold, medical surgical supplies and other categories should not be increased since the Hospital's charges in these areas are comparable with other Hospital's in the region. The charge level of these services is approximately 32% of the total charge structure of the Hospital. The remaining 68% of charges will be increased 6%.

Included in the Hospital's charge increase is a provision for Health Reform Initiatives. The Hospital is continuing with its Transitional Care Program. Included in the operating budget is approximately $667,000 related to this program. This program's mission is to assist in the management of high risk patients across the care continuum with the goal of decreasing emergency room visits, hospital admissions and readmissions. The most recent public information available has SVMC's 30 day readmission rate is 10.9% compared to the VAHHS data for the state of Vermont which is 16.6%. The second item included is approximately $700,000 for OneCare fees for FY 2016 which increased by over 100% for SVMC. In addition, there are costs included in the budget related to the Hospital's Community Needs Assessment which includes many smaller initiatives in the community. Included is the continued financial support to the local free clinic, wellness and community building initiatives, as well as support of the initiatives related to substance addiction and abuse.

Increase in Medicare rates

Included in the FY 2016 budget is an increase in Medicare reimbursement for inpatient and outpatient services. The update factor used for inpatient was 1.10%. The inpatient services assumption will be effective October 1, 2015. The update factor utilized for outpatient services will be 1% effective January 1, 2016. *Currently, there is* ***no*** *consideration included in the budget for potential changes in the Inpatient or Outpatient Prospective Payment rules or methodologies. These items are usually finalized after submission.*

Medicare SCH reimbursement

Included in the Hospital's FY 2016 budget is a full year of the Medicare SCH payments. Sole Community Hospital status was granted to SVMC by CMS on December 24, 2014. The increase in reimbursement over Medicare Dependent Hospital rates is approximately $2.2 million, annually.

Increase in Medicaid DSH payments

Medicaid DSH payments will decrease by $932,945 in FY 2016. This amount was confirmed in a letter received from the State of Vermont;

Decrease in indigent care

Total indigent care will decrease by $1,010,000 when comparing FY 2015's budget to FY 2016's budget.

FY 2015 charity care budget was $2.4 million and the projected amount is approximately $880,000 less then budget. Based upon the current activity and factoring in an anticipated change to the charity care program that would expand eligibility and increase scaled discounts that begin at the Medicaid payment levels for patients who meet eligibility the projected FY 2016 levels will be $2,000,000 or a positive variance of $360,000. As with charity care the FY 2015 projected bad debt expense is under budget in FY 2015. In FY 2016, management anticipates to see a reduction in the provision for bad debt partially due to the anticipated changes in the charity care policy that should encourage some patients to apply for charity care that might otherwise end up in bad debt cycle. In addition, increased effort to collect deductibles and coinsurance at the time of service should further reduce the number of accounts that end up in bad debt cycle.

Expanded access and enhanced services

SVMC's community needs assessment and monitoring primary care is an area which more resources are needed. Over the past years and in the FY 2016 budget SVMC is continuing, to add resources and address the primary care access shortfalls in Hospitals region. In the FY 2016 budget SVMC is budgeting to add primary care providers, associate providers and renovate facilities to improve access for patients in our service area.

Expanded access

Express Care (Bennington, VT) – As part of the primary care renovations in 2015, SVMC launched a same day appointment clinic to further provide primary care access and depressurize the emergency department. The clinic opened in February of 2015. In the FY 2015 budget this was planned to be open in October 2014. Express Care provides access to physicians and associate providers for patients with minor conditions. The operating hours are budgeted to increase in 2016. The clinic will be open seven days a week with extended hours on weekends. The projected visit volume with generate approximately $116,000 in additional net patient service revenues in FY 2016.

Bennington Family Practice (Bennington, VT) – SVMC is planning to integrate the former independent Family Practice providers into Dartmouth-Hitchcock Putnam Medical Group of SVMC and assume control of the practice in January of 2016. This medical home practice will lose a key provider to retirement in the coming months and as an independent practice, it is unable to recruit a replacement provider. Since the practice provides critical primary care to the region, especially in Bennington, SVMC is integrating the practice and recruiting a replacement provider. These efforts are essential to stabilize the local primary care network and ensuring that Vermonters can access primary care rather than utilize SVMC's emergency room services. Management projects the enhanced access to result in additional collectible revenues of $460,862.

Pownal Primary Care Clinic (Pownal, VT) – In March, SVMC broke ground on a new 5,200 sq. ft. facility along Route 7 in Pownal. This facility will house a medical home primary care practice lead by a team of family practice providers focused on improving the health of some of the most vulnerable residents in rural southern Vermont. The clinic will also serve communities in the southern portion of our service area, including Pownal and northern Berkshire County, MA. With the closing of North Adams Regional Hospital in March of 2014 the already limited access to open primary care practices and access to the providers has eroded creating a significant need. Progress on the facility is advancing, with scheduled opening in October. In the FY 2015 budget this site was due to open in July 2015 but due to the winter and challenges with the site it has been moved to October 2015. Patients, unable to access primary care elsewhere, have already begun calling requesting appointments for October. Management believes this access point will provide essential primary care to SVMC's southern service region. Pownal Primary Care was included in the FY 2015 budget submission with an anticipated July, 2015. The additional net revenue in the FY 2016 budget is $336,363.

Enhanced Services

Palliative Care Management (throughout our service area) – In January of 2015 SVMC began to offer palliative care. This service allows patients to receive care that cannot otherwise be provided by their primary care physician. Formalizing the care and referral process has enhanced the patient and family experience. We anticipate an increase in volume and collectable revenues of approximately $12,000.

Rheumatology – SVMC/Dartmouth-Hitchcock Putnam Medical Group has successfully recruited a rheumatologist to replace the independent physician that retired in 2014. Since 2014, SVMC has been utilizing locums to provide limited rheumatology services while engaged in targeted recruitment efforts. The rheumatology recruit will begin in August, 2015 and is currently in fellowship at Roger Williams Medical Center (Providence, RI) and is board certified in internal medicine and board eligible in rheumatology. Management has budgeted a revenue increase of $69,000 because the full-time provider will work through the back-log of patients that has developed for this service.

Neurology – SVMC/Dartmouth-Hitchcock Putnam has successfully recruited a neurologist to address the significant unmet neurology needs across our service area. The primary care practices through the region and SVMC's emergency department are challenged by patients requiring neurology consults and care. The need for a neurologist has been acute for several years, however recruitment has been difficult. The neurology recruit is currently completing her fellowship at Albany Medical Center and is board eligible. Management anticipates $300,000 in new revenue as this neurologist starts in August, 2015 and begins to work through the significant queue of patients

Allergy – Management is currently recruiting for a full-time Allergist to replace the part-time provider that recently retired. Providing access to quality allergy services is critical to identifying and managing allergies, particularly of children, that otherwise might result in use of the emergency department. Recruitment efforts are underway in earnest and management anticipates securing a recruit to being within FY 2016.

Volumes and payer mix

Inpatient volumes have decreased in FY 2015 compared to FY 2014 actual and the FY 2015 budget. The FY 2016 budget assumes the continued decline in the inpatient services due to the following:

- Continued improvement of the Hospital's readmission rate;
- Effectiveness of the Transitional Care Nursing program;
- Net change in inpatient operating room case volumes mainly due to the loss of two orthopedic surgeons and the timing of the recruitment of a replacement;

Outpatient volumes are mixed; however, in the budget the increase combined with the declines in the trend produces a net decline in revenues. Below summarizes the significant changes:

- The Emergency Room visits it is anticipated that the volumes will change slightly due to:

  - Decrease due to the opening of the Same Day Clinic and other efforts to expand primary care access;
  - Overall, trends at SVMC and environment.

- Same Day Surgery volumes will be less mainly due to due to the orthopedic surgeon vacancies and the timing of the recruitment of a replacement;

- Other ancillary volumes such as lab and imaging services (MRI, CT Scan and others) are anticipated to be consistent with projected FY 2015 volumes, up slightly from FY 2015 budget;

- Radiation Therapy procedures are anticipated to decrease from the FY 2015 budget but increase over the projected FY 2015 volumes due to program changes;

Operating Expenses

SVMC operating expenses are budgeted to increase by $4,859,625 or 3.55% compared to FY 2015 budget. During FY 2015 SVMC has made concerted efforts to reduce expenses in response to lower volumes in some areas and to prepare for anticipated healthcare reform.

Healthcare Reform Cost

SVMC's FY 2016 budget includes Healthcare reform costs of $2,177,000. Included in the budget is $667,000 for transitional care program. The purpose of the program is in assisting in the management of high risk patients across the care continuum with the goal of decreasing emergency room visits, hospital admissions and readmissions. This department includes clinical nurse specialists, pharmacist and social worker. Included in the budget is approximately $700,000 for ACO participation fees, $325,000 for further development of the DH affiliation and $485,000 for Berkley Research Group (BRG) operational efficiency initiative to help reduce SVMC's expense structure in FY 2016 and to prepare for the future payment reform models.

Salaries and wages -- non physician

The salaries and wages are budgeted to be basically at FY 2015 levels. In developing the FY 2016 salary and wage budget the effect of the FY 2015 wage increases was included as well as a 3% wage increase effective May 2016 was included.

The table below identifies the changes in salary and wage expense compared to the budgeted FY 2015 amount:

Compensation increase FY 2016	$1,309,325
Expanded and enhanced services—new FTE's	444,629
Others hospital and medical group changes	(56,201)
Total change (amounts rounded)	***$1,697,753***

Below is a summary of FTE's.

	FY 2015 Projected	***FY 2015 Budget***	***FY 2016 Budget***	***Variance Budget to Budget FTE***	***Variance Budget to Budget %***
Total SVMC (non-physician)	***735.6***	***734.6***	***747.9***	***13.3***	***1.8%***

Management will be monitoring the FTE's closely related to volumes in FY 2016.

Physician fee/salaries, contracts and fringes

This category of expense is increasing by $621,272 in FY 2016 when compared to the FY 2015 approved budget. The table below will provide some of the highlights to the changes in this classification of expense.

New providers and associate providers to improve access	$838,163
New providers to enhance services	764,704
Physician reductions – Orthopedics	(712,338)
Compensation rate changes and other reductions	(269,257)
Change in physician fee/salaries, contracts and fringes	***$621,272***

Employee Benefits

In the FY 2016 operating budget, employee benefits are targeted to increase $335,131 or approximately 2.8% over FY 2015 budget. The employee benefit expense represents approximately 27.1% of salary costs. The FY 2016 budget assumes continued favorable self-insured claims experience in both the employee health insurance program and workers compensation. In addition, there is a $1.1 million credit related to the defined benefit pension plan, reducing the employee benefit cost. Without this credit employee benefit expense would be over 29%.

Provider Tax

The absolute dollar amount of the increase over FY 2015 budget is $336,171 or 4.1%. The provider tax has *doubled* from $4,224,089 to $8,474,000 since FY 2009.

Depreciation and Amortization Expenses

The depreciation and amortization expense will be budgeted at $6,263,876 or an increase of approximately $17,000 over FY 2015's budget. This is based upon a FY 2016 Capital Budget of $17.160 million, an assumption that all FY 2016 capital budget will all be acquired as planned as well as the depreciation expense on assets currently in service.

The Capital Budget of approximately $17.160 million in FY 2016 will be funded from cash and cash generated from operations and borrowing. In summary, the Capital Budget is allocated as follows:

Large capital projects	$8,190,000
Large infrastructure projects	2,500,000
Routine information technology	1,000,000
Routine capital needs	5,470,000
Total	***$17,160,000***

Interest Expense

It is worth noting the FY 2015 capital budget of over $13 million will not be expensed due to delay and changes in plans in our strategic initiatives. Several items are carried forward and included in FY 2016 budget. Interest expense in FY 2016 is projected to increase by approximately $47,000 for the FY 2015 budget. In FY 2016 management is anticipating to borrow approximately $10 million to fund it capital budget. In the FY 2015 budget the borrowing assumption was $7 million which management did not execute.

Other operating expenses

Other operating expenses in the FY 2016 operating budget are increasing by $2,051,015 or approximately 5.0%. The table below highlights some of the significant changes:

	Amount
Administration	$1,282,522
Administration - Medical Group	421,154
Physician office practices	1,155,805
Emergency Room	406,195
Medical Care Evaluation	377,819
Pharmacy and drugs sold	(1,079,669)
Operation of plant	(457,378)
Medical surgical supplies sold	(261,271)
All others	178,857
Total increase	***$2,051,015***

- Administration – OneCare fees increasing $350,000, additional DH affiliation costs of $325,000 and cost related to operational efficiency initiative with Berkley Research Group (BRG) of $485,000;
- Administration - Medical Group – cost related to additional resources focused on improving operational efficiencies;

- Physician office practice – additional expenses related to new and enhanced medical group practices;
- Emergency Room - costs related to contract labor and Scribe program ($300,000) to improve documentation and physician efficiency;
- Medical Care Evaluation – primarily related to increased efforts to monitor quality as SVMC implements operational efficiency initiatives and organizational change to prepare for health care reform;
- Pharmacy drugs sold – savings related to the 340b program;
- Operation of plant – savings from completed and planned energy efficiency initiatives;
- Medical surgical supplies sold – reduced expenses due to anticipated decline in orthopedic surgical volume.

Greater detail can be provided upon request.

Proposed or Potential Certificate of Need (hereafter "CON")

SVMC is currently completing a CON application for a Linear Accelerator for the Cancer Center, modifications to the physical plant, information systems improvements and emergency room renovations. While no firm plans have been developed for each of these projects that would require CON approval, management estimates the capital costs of these projects to be:

• Linear Accelerator FY 2015-2016	$3,940,000
• Boiler Plant Modernization FY 2015-2016	3,500,000

These amounts are above the routine capital of the organization which has ranged from $5.5 million to $7.0 million per fiscal year.

Management in the coming years will be evaluating significant changes to the physical plant of the Medical Center and changes to its current compute platform. Estimates are not available at this time.

Non-operating gains and losses

The non-operating gains and losses are mainly out of the control of management. Investment earnings on the funded depreciation are driven by market and economy. No gain or loss on the interest rate swap was budgeted. The budget also includes $250,000 of contribution income.

* * * * * *

If there are any questions or comments please do not hesitate to contact Stephen D. Majetich, Chief Financial Officer at 802.447.5011